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OFFICE OF INSPECTOR GENERAL

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OCT 30 2003

Control Number ED-OIG/A05-D0018

Sister Judy Bisignano, Ed.D.
Cesar Chavez Middle School
3372 S. 6th Avenue
Tucson, AZ 85713

Dear Sister Bisignano:

This **Final Audit Report** presents the results of our audit of the Cesar Chavez Middle School's (School) use of U.S. Department of Education (ED) funds for the period July 1, 2001, through June 30, 2002 (2001-2002 fiscal year). The objective of our audit was to determine if the School expended ED funds according to applicable law and regulations.

Our audit disclosed that the School did not expend Public Charter Schools Program (PCSP) funds in accordance with the law. The School received \$200,000 in PCSP funds for its 2001-2002 fiscal year but did not provide documentation supporting its use of \$183,706. Of the \$16,294 for which it provided documentation, the School used \$13,099 for costs that were unallowable.

We provided a draft of this report to the School. However, the School did not provide us with comments.

AUDIT RESULTS

Finding No. 1 The School Could Not Support Its Use of \$183,706 in PCSP Funds

The School did not provide (1) complete and accurate accounting records that fully showed how it used PCSP funds and (2) documentation that was sufficient to support its use of \$183,706¹ in PCSP funds. For the 2001-2002 fiscal year, the School received \$200,000 in PCSP funds. When we asked for records showing how the School used the PCSP funds, School officials originally provided accounting records that showed only \$150,899 was charged to the PCSP grant. We judgmentally² selected three drawdowns totaling \$94,535 made prior to December 31, 2001, and three individual expenses totaling \$5,237 posted after December 31, 2001, and asked School officials to provide us with

¹ \$200,000 received less \$16,294 in expenses for which we received documentation.

² See the Objective, Scope, and Methodology section of this report for an explanation of our sample selection.

supporting documentation (requisitions, purchase orders, invoices, and canceled checks). The documentation the School provided was sufficient to support its use of only \$16,294.

We informed the School that its records were not sufficient to show how it used all its PCSP funds. The School's Director assured us that the School used all \$200,000 in PCSP grant funds received for the 2001-2002 fiscal year for PCSP purposes and provided us with revised accounting records. The revised accounting records showed that the School charged \$221,439 to the PCSP grant, \$21,439 more than the School received. When we asked for documentation supporting the School's use of the \$200,000 in PCSP grant funds it received for the 2001-2002 fiscal year, School officials did not provide us the records needed to support \$183,706.

According to 34 C.F.R. § 75.730,³ direct grant recipients are required to keep records that fully show the amount of funds under the grant, how the grantee uses the funds, the total cost of the project, the share of that cost provided from other sources, and other records to facilitate an effective audit.

School officials had a difficult time maintaining and accessing records for the 2001-2002 fiscal year. During the 2001-2002 fiscal year, the School used two different financial services companies to maintain its financial management system. When the second financial services company started to perform services for the School, the company made several adjustments to the School's accounting records. In an attempt to provide us with complete and accurate accounting records for the 2001-2002 fiscal year, School officials worked with the second financial services company and had the company make adjustments to the School's accounting records. Despite its efforts, the School could not provide us with complete and accurate accounting records and related documentation that was sufficient to support its use of all PCSP funds. It could not provide us with accurate records and sufficient documentation because the School did not have policies and procedures to ensure that its accounting records were reconciled on a regular basis and accurately reflected the School's use of PCSP funds.

Without complete and accurate accounting records and supporting documentation, we could not determine whether the School expended \$183,706 of PCSP funds according to the law and applicable regulations.

Recommendations

We recommend that the Chief Financial Officer, Office of the Chief Financial Officer, in conjunction with the Deputy Under Secretary for the Office of Innovation and Improvement, instruct the School to

- 1.1 refund \$183,706 to ED; and
- 1.2 develop and implement policies and procedures for regularly reconciling the amount of PCSP funds received with the amount spent.

³ Unless otherwise specified, all regulatory citations are to the July 1, 2001, volume.

Finding No. 2 The School Charged Unallowable Costs to the PCSP Grant

For the 2001-2002 fiscal year, the School charged \$13,099 to the PCSP grant for costs that were unallowable under the law. For its 2001-2002 fiscal year, the School received \$200,000 through 25 draws from ED's Central Automated Processing System, Grant Administration and Payment System. The accounting records that School officials originally provided us showed that the School charged only \$150,899 to the PCSP grant for the 2001-2002 fiscal year. We judgmentally selected three drawdowns totaling \$94,535 and three individual expenses totaling \$5,237 recorded in the School's system of records.⁴ School officials only provided us with documentation sufficient to support \$16,294 (\$13,099 in drawdowns and \$3,195 in individual expenses). We reviewed the documentation and determined that \$13,099 was used for overnight fieldtrips for students and one piece of artwork. These costs were not related to the initial implementation of the School. The costs were general operational costs, not initial operational costs that could not be met by other sources.

The Elementary and Secondary Education Act of 1965, as amended by the Improving America's Schools Act of 1994, Title X, Part C, Section 10304(f)(3), and the Charter School Expansion Act of 1998,⁵ allows charter schools to spend funds for activities related to post award planning and design of the educational programs and initial implementation of the charter school. Activities related to initial implementation may include (a) informing the community about the school, (b) acquiring necessary equipment and educational materials and supplies, and (c) acquiring or developing curriculum materials. Charter schools are allowed to pay for other initial operational costs not met by other sources provided that those costs are directly related to the purpose of the PCSP grant. The intent of the PCSP grant is to pay for necessary items and services that would support the initial implementation and operations of the school while also allowing the school to become financially independent.

The School charged unallowable costs to the PCSP grant because it did not have policies and procedures in place to provide reasonable assurance that PCSP funds were expended on activities allowable under the law. A School official stated that the School received special approval from ED's Charter School office to expend PCSP funds for student fieldtrips as part of its educational program. However, the School official was unable to provide documentation of the approval. Additionally, School officials were unable to provide an explanation why artwork was purchased with PCSP funds.

⁴ Because the School ended its contract with one financial services company on December 31, 2001, and hired a new financial services company effective January 1, 2002, we selected three drawdowns made prior to December 31, 2001, and three individual expenses recorded after January 1, 2002. The original accounting records that School officials provided us showed that the School's PCSP expenditures totaled \$150,899 for the 2001-2002 fiscal year. However, its detailed ledger was incomplete and inaccurate. Therefore, we could not determine the exact number of expenses charged to the grant for the 2001-2002 fiscal year.

⁵ The law was further amended by the No Child Left Behind Act of 2001, Title V, Part B.

Because School officials used \$13,099 in PCSP funds to pay for general operational costs, the School was unable to use those funds to purchase items that would increase the chances of the School becoming financially independent.

Recommendation

We recommend that the Chief Financial Officer, Office of the Chief Financial Officer, in conjunction with the Deputy Under Secretary for the Office of Innovation and Improvement, instruct the School to

2.1 refund \$13,099 to ED for unallowable costs charged to the PCSP grant.

BACKGROUND

The purpose of the PCSP grant is to provide grants for the planning, design, and initial implementation of charter schools created by members of the local community. Grants may be made for a period of up to three years. Funds may be used to plan and design the education program of the charter school and evaluate the effects of charter schools.

Charter schools are governed by the charter school legislation enacted in the Elementary and Secondary Education Act of 1965, as amended by the Improving America's Schools Act of 1994, Title X, Part C, Section 10304(f)(3), and the Charter School Expansion Act of 1998. Charter schools that receive a grant directly from the federal government must also adhere to regulations listed in 34 C.F.R. Parts 75, 82, and 99.

The School received its charter from the Higley School District and opened in August 1999. The School applied for a PCSP grant and received approval from ED on August 19, 1999. The grant provided the School with startup funding for a three-year period. For the 2001-2002 fiscal year, the third year of funding, the School received \$200,000.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our audit was to determine if the School expended ED funds according to applicable law and regulations. For the purpose of this report, our audit covered the PCSP award ED made on September 12, 2001, for \$200,000 and costs charged to the grant for the 2001-2002 fiscal year.

To accomplish our objective, we

- interviewed School personnel and third party vendors hired by the School;
- obtained and reviewed accounting records;
- judgmentally selected three drawdowns totaling \$94,535 made prior to December 31, 2001, and three individual expenses totaling \$5,237 posted after December 31, 2001. We selected the drawdowns because the School did not provide us with a list of expenses charged to the grant before January 1, 2002. We selected expenses posted

after December 31, 2001, with large dollar amounts and/or cost descriptions that were vague or inconsistent with the PCSP law.

- compared purchase orders, invoices, and canceled checks with the School's accounting records to determine whether expenses charged to the PCSP grant were supportable and allowable.

As part of our audit, we used computer-processed data contained in the School's accounting records. We could not determine the reliability of this data because the School provided us with two versions of its accounting records that showed it spent different amounts of PCSP funds for its 2001-2002 fiscal year. In addition, the School was unable to provide us documentation that would support its use of PCSP funds. However, we used the computerized accounting records for the limited purposes of our audit because it was the only information provided that showed how the School used PCSP funds.

We performed our audit work between December 2002 and July 2003. We visited the School on December 9, 2001, and discussed the results of our audit with School officials on March 27 and April 17, 2003.

Our audit was performed in accordance with generally accepted government auditing standards appropriate to the scope of audit described above.

STATEMENT ON MANAGEMENT CONTROLS

As part of our audit, we did not assess the adequacy of the School's management controls applicable to all ED awards because this step was not necessary to achieve our audit objective. Instead, we relied on our testing of the School's compliance with the law and applicable regulations. Our testing disclosed material weaknesses in the School's management controls over PCSP awards. The School did not have policies and procedures in place to (1) ensure that its accounting records were reconciled on a regular basis and accurately reflected the School's use of PCSP funds and (2) provide reasonable assurance that PCSP funds were expended on activities allowable under the law. These weaknesses are discussed in the **AUDIT RESULTS** section of this report.

ADMINISTRATIVE MATTERS

Statements that managerial practices need improvements, as well as other conclusions and recommendations in this report, represent the opinions of the Office of Inspector General. Determinations of corrective action to be taken will be made by the appropriate ED officials.

If you have additional comments or information that you believe may have a bearing on the resolution of this audit, you should send them directly to the following ED officials, who will consider them before taking final Departmental action on this audit.

Jack Martin, Chief Financial Officer
Office of the Chief Financial Officer
U.S. Department of Education
400 Maryland Avenue, SW, Room 4E313
Washington, DC 20202

Nina Shokraii Rees, Deputy Under Secretary
Office of Innovation and Improvement
U.S. Department of Education
400 Maryland Avenue, SW, Room 4W317
Washington, DC 20202

It is ED's policy to expedite the resolution of audits by initiating timely action on the findings and recommendations contained therein. Therefore, receipt of your comments within 30 days would be greatly appreciated.

In accordance with the Freedom of Information Act (5 U.S.C. §552), reports issued by the Office of Inspector General are available to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act.

Sincerely,

A handwritten signature in black ink, appearing to read 'Richard J. Dewd', with a large, stylized flourish at the end.

Richard J. Dewd
Regional Inspector General
for Audit